

DEFENSE LOGISTICS AGENCY
Defense-Wide Working Capital Fund
Defense Reutilization and Marketing Service
FISCAL YEAR (FY) 2004 BUDGET ESTIMATES
February 2003

FUNCTIONAL DESCRIPTION

The Defense Logistics Agency (DLA) Defense Reutilization and Marketing Service (DRMS) Activity Group is responsible for the reuse, or reutilization, of excess and surplus personal property within the Department of Defense (DoD). DoD inventory managers submit requirements to DLA via automated requisitions using standard requisition and issue procedures. Items received by the DLA Defense Reutilization and Marketing Offices (DRMOs) meeting Military Services item manager criteria are automatically referred through front-end screening notices. The Military Services reutilized 1.23 billion worth of personal property in FY 2002, resulting in savings to the DoD and the Government. If property is not reutilized, it can be transferred to other Federal agencies. Remaining property becomes surplus and is made available for donation to authorized state agencies and charitable organizations. The balance of property is offered for competitive sale to the public.

The DLA disposal mission includes hazardous property disposition. In this capacity, DLA handles the vast majority of DoD property governed by the Resource Conservation Recovery Act (RCRA) of 1976, as amended. Some hazardous material has reutilization and/or sales value and goes through the same process as all other DoD property. However, once it has been screened for potential reutilization or sales value, all hazardous waste is directly disposed of through contracts managed by DLA and direct funded by the Military Services.

DRMS headquarters, responsible for operational control, is located in Battle Creek, Michigan. The operational core of this organization lies with individual DRMOs located on military installations throughout the world. DRMOs receive, classify, segregate, demilitarize, account for and report excess material for screening, lotting, merchandising, and sales.

CHANGES IN OPERATIONS

DRMS has adopted a corporate strategy of focusing, managing, and measuring logistics support based on customer needs; consistently providing responsive, best value supplies and services to their customers. DRMS is transitioning from being geography based to customer needs based.

Workload projections were reviewed and revised based on input from DRMS generators as well as from the DRMS National and International Commands. The Services are doing a better job of managing their inventories and thus generating less excess property; therefore, a decline of workload is reflected, 5 percent decrease from FY 2002 through 2004 in acquisition value and a 7 percent decrease in line items. We anticipate workload continuing to decline through FY 2004 and leveling off in the outyears. However, these workload projections could be impacted by returns from Operation Enduring Freedom and any new rounds of BRAC closures.

In addition to the decline in the volume of workload, the quality of property received has also fallen. This drop in quality as well as changes to the computer hard drive policy have lead to more property being downgraded to scrap upon receipt. While these factors negatively impact the percent of property reutilized, transferred, and donated, they have a bigger impact on the amount of usable property available for sale. Therefore, there have been some adjustments within all the Business Units workload projections. Revenue projections have been adjusted to reflect the higher downgrade to scrap rate and a downturn in the scrap market.

DRMS also conducted an A-76 public/private competition on the logistics stock, store and issue functions at 10 DRMOs. The first DRMS A-76 competition was completed in FY 2000 and resulted in the conversion to contract of the affected functions. DLA announced on October 9, 2001, the second DRMS A-76 study of the warehouse logistics functions at the 61 CONUS DRMOs. Approximately 319 FTEs were impacted. We expect decisions on this second round in the first quarter of FY 2004. FTE and labor savings budgeted include only most efficient organization (MEO) savings. Costs and savings are prorated to the fiscal year in which they are expected to occur.

DRMS has a long-range goal of becoming a broker of information which will result in the more efficient management of property. Their initiatives have been focused on enacting process improvements that will allow achievement of this goal. As DRMS transitions to an organization that is more adept at "moving information and not property", DRMS will be able to centralize its organizational presence at fewer strategic locations. This will allow DRMS to effectively perform its mission with substantially reduced infrastructure, labor and cost.

BUDGET HIGHLIGHTS

TRANSACTION ACTIVITY BILLING:

Historically, DRMS has recovered operating costs with a combination of proceeds from the sale of surplus personal property to the public, reimbursements from specific customers for work performed and a Service Level Billing (SLB) paid by the Military Services and DLA Supply Management Activity Groups. DLA developed Transaction Activity Billing (TAB) to recover mission costs based on actual services and workload for property disposition. Estimated workload and cost data are processed through the TAB model. Through this process DRMS can identify the end user and the working capital fund customer separately, providing visibility of the disposal cost in the life cycle of the item.

TAB is a practical application of Activity Based Costing (ABC) principles to assess costs and set billing rates in accordance with the level of effort required to perform the service. We have used the TAB application workload estimates to determine customer funding levels. Customer service level billings based on previous budget determinations and this budget request are as follows:

<u>Dollars in Millions</u>				
Customer	<u>FY 2002</u>	<u>FY 2003</u>	<u>FY 2004</u>	<u>FY 2005</u>
Army	81.5	93.8	77.0	67.9
Navy	64.1	56.5	51.7	45.5
Air Force	45.8	39.8	36.1	31.8
DLA	<u>44.1</u>	<u>36.1</u>	<u>43.8</u>	<u>38.6</u>
Total	235.5	226.2	208.6	183.8

UNIT COST/PERFORMANCE INDICATORS:

This submission includes a redesign to the DRMS unit cost structure. The previous structure captures all costs of providing compliant disposal services to DoD. However, it does not capture all the workload associated with the disposal process. In recent years there has been a distinct downward trend in the value and marketability of excess property being turned in for disposal. This trend is consistent with ongoing DoD and DLA supply chain strategies and is particularly visible in the Reutilization, Transfer, and Donation (RTD) and sales programs. The new unit cost structure: (1) captures additional workload elements - line items of useable property received; (2) changes workload indicators for RTD and sales from dollars to lines; (3) eliminates Abandonment and Destruction and replaces it with Recycling/Disposal that captures all recycling processes (scrap, demilitarization, mutilation and demanufacturing; and (4) changes the name of Ultimate Disposal to Hazardous Waste Disposal.

The DRMS unit cost goals are based on the major work processes:

- a. **Receiving** unit cost goal is based on the total cost associated with the receiving process for useable property divided by the number of line items of useable property received.
- b. **Reutilization/Transfer/Donation (RTD)** unit cost goal is based on the total cost associated with the RTD process divided by line items of property disposed via RTD.
- c. **Sales** unit cost goal is based on all costs associated with the public sale of surplus personal property divided by the number of line items of property sold.
- d. **Hazardous Waste Disposal** unit cost goal is based on the non-contract costs associated with environmentally regulated disposal of hazardous waste divided by the number of pounds of hazardous waste disposed.
- e. **Recycling/Disposal** unit cost goal is based on the cost of either storing in a landfill or destruction of those non-hazardous items that remain at the end of the disposal process as well as the cost of all recycling processes divided by the number of pounds of property disposed.

Costs are allocated using an ABC Model. DRMS updates and refines the ABC Model during each budget submission to more accurately capture costs and bill their customers based on the actual services provided to them. DRMS earns its obligation authority through unit cost goals. The FY 2002 actual and FY 2003 through FY 2005 estimated goals and workload are reflected below:

Unit Cost

	FY 2002 Actual	FY 2002 Workload
R/T/D <u>1/</u>	\$0.0380	\$1,717.5
Sales <u>1/</u>	\$2.3724	\$39.7
Ultimate Disposal <u>2/</u>	\$0.181	212.5
Abandon & Destruct <u>2/</u>	\$0.088	101.8

1/ Workload in millions of dollars

2/ Workload in millions of pounds (Performance Indicator)

Revised Unit Cost Structure

	FY 2003 Goal	FY 2003 Workload	FY 2004 Goal	FY 2004 Workload	FY 2005 Goal	FY 2005 Workload
Receiving	\$24.458	2.903	\$25.404	2.787	\$24.380	2.703
R/T/D 1/	\$268.023	.172	\$268.023	.174	\$275.926	.162
Sales 1/	\$55.890	.399	\$55.890	.357	60.969	.351
Haz Waste Disp 2/	\$0.203	197.300	\$0.203	191.700	\$.207	186.3
Recycling/Disp 2/	\$0.056	843.700	\$0.056	742.100	\$.070	651.6

1/ Workload in millions of lines received

2/ Workload in millions of pounds (Performance Indicator)

Workload:

During FY 2002, DRMS continued to experience a reduction to reutilization workload. The main driver for this decline was the GSA moratorium on transfers of excess computers to UNICOR, which accounted for \$1 billion in RTD workload in FY 2000. DRMS continues to see the effects of this moratorium. Also the DoD policy requiring destruction of unclassified computer hard drives prior to release outside of DoD precluded disposal by RTD. Subsequently, this policy was revised but still has a negative impact on workload. As a result, RTD workload for FY 2002 was \$1.7 billion below our original estimate of \$2.98 billion. Starting in FY 2003 RTD workload will be measured by line items disposed via the RTD process. We estimate a 6% decrease in workload over the budget period.

Sales continue to decline as a result of lower turn-ins and decreased value of property that is turned in. Over the past several years DRMS estimated workload (measured in latest acquisition value of useable property turned in for disposal) to decrease 12 percent but have actually experienced a 35 percent reduction. Useable property may be downgraded to scrap upon receipt based on the condition and value of the property. The downgrade rate was projected at 48 percent of useable receipts. Based on current experience the downgrade rate is now 59 percent. The increased downgrade rate reflects the declining value of the property which negatively impacts sales proceeds. Starting in FY 2003 Sales workload will be measured in lines sold. Despite the market value of the property, DRMS incurs the same cost to sell. Lines are a better measure of the work effort.

Hazardous Waste Disposal and Recycling/Disposal workload show a decrease from FY 2002 to FY 2004, 6 percent and 23 percent respectively, due to the overall reduction in disposal workload.

NET OPERATING RESULT (NOR)/ACCUMULATED OPERATING RESULT (AOR)

In FY 2002, DRMS experienced an NOR gain of \$56.9 million. This gain will partially offset the AOR loss brought forward from the FY 2001 revenue loss incurred. This loss was the result of an unsuccessful legislative proposal to allow the transfer of revenue from the Defense National Stockpile Center to DRMS. During FY 2003, we are projecting an NOR gain of \$41.4 million to offset the AOR loss from FY 2002 due to lost revenue from sales. For FY 2004 DRMS costs not covered by other revenue (sales, reimbursable projects) will be recovered through TAB rates.

NOR/AOR
(\$ in Millions)

	<u>FY 2002</u>	<u>FY 2003</u>	<u>FY 2004</u>	<u>FY 2005</u>
Revenue	\$356.2	\$333.5	\$307.6	\$279.9
Expenses	\$299.3	\$292.1	\$296.2	\$279.9
Operating Result	0.0	0.0	0.0	0.0
Other Changes Affecting NOR	0.0	0.0	0.0	0.0
NOR	56.9	41.4	11.4	0.0
Prior year AOR	(109.7)	(52.8)	(11.4)	0.0
Non-Recoverable Adjustment				
Impacting AOR	0.0	0.0	0.0	0.0
AOR	(52.8)	(11.4)	0.0	0.0

MILITARY AND CIVILIAN PERSONNEL

Reductions in employment levels, without degradation of mission support, are achieved primarily by automation and management improvements. Automating the reutilization and marketing processes and management information systems (moving information not property) reduces the need for manual intervention. As DRMS transitions into moving more information and less property, they will be able to centralize their organizational presence at fewer strategic locations with substantially reduced infrastructure, labor and cost. Productivity measures include the number of people employed or, more importantly, the full-time equivalents used. The table identifies budget estimates for full-time equivalents and end strength for DRMS and corporate allocations. Full Time Equivalents are coming down 12% over the budget period.

Military and Civilian Personnel

	<u>FY 2002</u>	<u>FY 2003</u>	<u>FY 2004</u>	<u>FY 2005</u>
End Strength				
Military	9	9	9	9
Civilian	<u>1,764</u>	<u>1,717</u>	<u>1,579</u>	<u>1,514</u>
Total	<u>1,773</u>	<u>1,726</u>	<u>1,588</u>	<u>1,523</u>
Full-time Equivalents				
Military	9	9	9	9

Civilian	<u>1,984</u>	<u>1,749</u>	<u>1,641</u>	<u>1,541</u>
Total	<u>1,993</u>	<u>1,758</u>	<u>1,650</u>	<u>1,550</u>

CAPITAL EXPENDITURES

DRMS monitors the condition of facilities and equipment at 95 DRMOs to maintain a safe and healthy workplace in accordance with stringent environmental and safety and health regulations. In FY 2004 and FY 2005, DRMS will replace tool carriers that have reached or exceeded their useful life at various DRMOs and replace existing Private Branch Exchange (PBX) systems at DRMOs Lewis and Norfolk. The Disposal Automated Information System (DAISY) changes will improve access and analysis of financial transactions from the receipt and disposal process. Improved access to DRMS financial information is critical to increasing the accountability of the disposal property, providing better information for decision-making, and increasing the efficiency and effectiveness of the services provided by DRMS. Minor Construction projects are to enhance operations at various storage facilities to promote proper handling of hazardous materials, hazardous waste, and items requiring demilitarization. Minor construction projects in FY 2004 and FY 2005 will alter facilities to accommodate mission consolidation and relocation, renovate demilitarization facilities, upgrade security facilities, and add paving for open storage, road networks, and parking. The table below depicts the capital program budget authority for FY 2002 through FY 2005:

Capital Program Budget Authority (\$ in Millions)

	<u>FY 2002</u>	<u>FY 2003</u>	<u>FY 2004</u>	<u>FY 2005</u>
Non-ADP Equipment	\$1.6	\$0.8	\$0.5	\$0.5
ADP Equipment	0.6	0.0	0.2	0.2
Software Development	3.0	1.3	2.0	1.0
Minor Construction	<u>3.0</u>	<u>6.0</u>	<u>5.0</u>	<u>3.0</u>
Total	<u>\$8.2</u>	<u>\$8.1</u>	<u>\$7.7</u>	<u>\$4.7</u>

DEFENSE LOGISTICS AGENCY
Defense Wide-Working Capital Fund
Defense Reutilization and Marketing Service
FISCAL YEAR (FY) 2004 BUDGET ESTIMATES
Source of New Orders and Revenue

(Dollars in Millions)

	FY 2002	FY 2003	FY 2004	FY 2005
1. New Orders				
a. Orders from DoD Components	305.2	280.2	262.6	237.8
Army	101.3	112.2	96.5	87.4
Navy	98.9	76.1	71.2	65.0
Air Force	58.2	50.7	48.3	44.0
Other	46.8	41.1	46.5	41.3
b. Orders from Other Fund Activity Groups	7.6	10.9	6.2	6.3
c. Total DoD	312.8	291.1	268.8	244.1
d. Other Orders:	3.7	3.7	3.7	3.7
Other Federal Agencies	0.7	0.7	0.7	0.7
Foreign Military Sales	3.0	3.0	3.0	3.0
Total New Orders	316.5	294.8	272.5	247.8
2. Carry-In Orders	0.0	0.0	0.0	0.0
3. Total Gross Orders	316.5	294.8	272.5	247.8
4. Sales Proceeds	39.7	38.7	35.1	32.1
5. Total Gross Sales	356.2	333.5	307.6	279.9

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Revenue and Expenses
February 2003
(Dollars in Millions)

	FY 2002	FY 2003	FY 2004	FY 2005
Revenue				
Sales				
Operations	356.2	333.5	307.6	279.9
Total Income:	356.2	333.5	307.6	279.9
Expenses				
Salaries and Wages:				
Military Personnel Compensation & Benefits	1.1	0.8	0.8	0.8
Civilian Personnel Compensation & Benefits	91.4	100.7	111.8	105.9
Travel & Transportation of Personnel	5.2	4.8	4.6	4.8
Materials & Supplies (For Internal Operations)	0.6	2.4	2.2	2.4
Equipment	3.5	9.5	9.0	6.4
Other Purchases from Revolving Funds	15.2	21.0	20.0	18.6
Transportation of Things	18.5	15.0	11.0	11.0
Depreciation - Capital	10.4	10.7	9.2	8.7
Printing and Reproduction	0.2	1.0	1.1	1.1
Advisory & Assistance Services	0.0	0.3	0.3	0.3
Rent, Communication, Utilities & Misc. Charges	6.0	5.1	4.8	4.8
Other Purchased Services	147.2	120.8	121.4	115.1
Total Expenses	299.3	292.1	296.2	279.9
Operating Result	56.9	41.4	11.4	0.0
Adjustments Affecting NOR/AOR	0.0	0.0	0.0	0.0
Net Operating Result	56.9	41.4	11.4	0.0
Prior Year Adjustments -- Prior Year AOR	-109.7	-52.8	-11.4	0.0
Other Changes Affecting AOR	0.0	0.0	0.0	0.0
Accumulated Operating Result	-52.8	-11.4	0.0	0.0
Non-Recoverable Adjustment Impacting AOR	0.0	0.0	0.0	0.0
Accumulated Operating Result for Budget Purposes	-52.8	-11.4	0.0	0.0